The US Election: Allocating for a Trump or Clinton Win

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In an information age where private or secret matters can readily be made public and reach critical mass via social media, opinions and perceptions can turn quickly. With less than a week left before Americans go to the polls, the outcome of who will become the next US president is still open. Furthermore, this election's polarised mood and rhetoric is pushing a divided electorate further into the extremes of the left and right-wing camp, leaving a large number of turned-off and undecided voters. They may not vote at all or, if they do, then it'll likely be on the final days approaching 8 November. Polls and betting odds too, currently favouring Clinton, can still mislead, no matter how obvious the current sentiment around a vote may be – just look at the UK 2015 general election or this year's EU referendum as examples.

Given the prevailing uncertainty around the US election, we offer a generic tactical and strategic asset allocation perspective on how a Clinton win could compare to a Trump win, by contrasting some of the potential reactions to major asset classes (see Figure 1). Underpinning such potential market reaction to the distinct investor perceptions of both candidates' policy agendas are:

(1) Short term: risk sentiment and Fed monetary policy decision

(2) Longer term: US fiscal and domestic policy (mainly on fiscal, trade and immigration)

Figure 1: Generic overview of how the US election could impact major asset classes

Positioning around US Election

		Short Term		Long Term	
	Asset Class	Market impact	Strategy	Market impact	Strategy
Trump	Equities	Volatile	Hedge / short broad exposures	Bullish US domestic growth	Small-Cap / Quality Growth
	Fixed Income	Low expectation of December Rate Hike	Bullish US Treasuries	More monetary tightening, more Fiscal easing	Bearish US Treasuries
	Currencies / Commodities	Risk-Off	Bearish Dollar, Bullish Gold	Stronger USD fundamentals	Bullish Dollar, Bearish Gold
Clinton	Equities	Stable	Defensive / Low beta	Bullish US Exports and trade	Equity Income, exporters
	Fixed Income	High expectation of December Rate Hike	Bearish US Treasuries	Soft monetary tightening, Soft fiscal easing	Bullish US Treasuries
	Currencies / Commodities	Risk-On	Bullish Dollar, Bearish Gold	Weaker USD fundamentals	Bearish Dollar Bullish Gold

Figure 2 summarises the contrast in tactical positioning around a Trump vs Clinton win using the most relevant short and leveraged ETPs, in our view.

Figure 2: Overview of how short and leveraged ETPs may be used to position tactically around equities, fixed income, currencies and commodities

If Trump wins: initial risk-off positioning, followed by upbeat equity market outlook

If Donald Trump wins, the markets in the US and overseas may experience an initial sell-off, as betting odds in mid-October were likely underestimating the chances of a Trump victory. With a President-elect Trump, greater volatility in stock and bond markets is likely, if only because there is much greater uncertainty about where the country will be headed and how it will be governed. His seemingly isolationist policy stance on immigration and transatlantic trade and military alliance is adding to the uncertainty.

Investors should consider hedging equity exposure through shorting and buying market volatility, or allocate into safe havens initially. When the dust settles, the lower valuations of domestic focused equity exposures are likely to gain appeal.

If Clinton Wins – Initial resilience of risk sentiment, defensive and exporters to benefit longer term

If Secretary Clinton wins, and the Republicans maintain control of at least the House of Representatives, many of her campaign promises will be dead on arrival. We will likely see something similar to a third

Obama term with respect to domestic policy — that is, gridlock in Washington on the legislative front, more activism on the regulatory and judicial fronts, tolerance of the status quo with respect to legal and illegal immigration, and continued institutional support for the global trading system and for America's strategic commitments overseas that help sustain it. That is, we could see continued slow growth in gross domestic product (GDP), stalled productivity and labour participation growth and perhaps another 12 to 18 months left in the current expansion, against a relative stable backdrop of international trade and military ties between the US and its Western partners, which should alleviate concerns over geopolitical tensions.

Investors may consider overweighting equities relative to bonds, especially when, amidst resilient risk sentiment, there is little that stands in the way for an ongoing build up in Fed rate hike expectations for December. Hedging US fixed income through short exposures in the underlying may be warranted initially. Longer term, there may be appeal for export-biased equities amidst slowing US growth and weaker fundamentals for the dollar.

Monetary policy: it trumps domestic policy short term

Generally, absent a foreign policy crisis, monetary policy and global macro forces will continue to have a bigger impact on markets than domestic policy. The impact that 535 lawmakers and one president have on the economy is often far less than the economic choices made by 320 million individual Americans. Changes in fiscal, tax, energy, education, health and regulatory policy all matter when measured over years or decades. But in the near term, the next six to 12 months, they have only an indirect impact on the direct inputs that move asset prices: interest rates, corporate profits, the dollar and the price of oil.

This is another way of saying that short term, equity and fixed income markets will be impacted more by US fundamentals, driven primarily by the Fed which will seek to calibrate the speed of expected interest rate increases to risk sentiment and global macro uncertainties. Hence, a Clinton win may help the Fed to initially trigger a rate hike faster than if a win by Trump would result in heightened market uncertainty, in which case the December rate hike may be delayed.

Fiscal policy: a major tool to direct the course of US economic performance by Trump or Clinton

The answer to the question "What impact would Trump or Clinton have on the economy?" comes down to what legislation House speaker Paul Ryan wants to introduce, what he believes can pass in the House and Senate and what a new president would ultimately sign. If Trump is elected, it's likely that the preferred path forward for Speaker Ryan will be broad tax reform that lowers tax rates for individuals and businesses, encourages private investment in the US, provides incentives for companies to repatriate foreign profits and, to the extent possible, curbs growth in future entitlement spending. A cut in the corporate tax rate could immediately increase the profits generated by corporate America, which could send stock prices higher. If Secretary Clinton is elected, there is a chance for a smaller fiscal package that could combine additional infrastructure spending with international tax reform that encourages companies to repatriate profits. But a larger budget deal next year that includes tax increases to reduce the federal budget deficit, similar to what President Bill Clinton achieved in 1993, remains unlikely with a Republican House, unless the package is overwhelmingly skewed toward spending cuts.

If the Democrats win back both houses of Congress and Secretary Clinton wins, the US stock market is likely to correct from present levels, discounting the possibility of new tax hikes in 2017. The more probable outcome is that the Republicans hold at least the House, and therefore a President Hillary Clinton will face major challenges to pass the higher tax rates she has proposed on capital gains, estates, financial transactions, higher incomes and carried interest. However, bi-partisan support may well exist for lowering the corporate tax rate on foreign profits. Such a tax cut would actually incentivise companies to bring back foreign cash into the US and could be a source of new tax revenue for the Federal government. Congressional Democrats could support such a measure, especially if it is coupled with greater infrastructure investment, something Secretary Clinton has advocated. With more than $2 trillion in corporate cash stashed overseas, companies could use such repatriated profits to increase hiring or capital spending, or more likely, to increase dividend payments and share repurchases.

Playing the domestic growth vs defensive story for equities longer term

Much of that overseas cash is concentrated in US multinational technology, healthcare, industrial, and global financial companies. A predominately large-cap ETF which provides investors exposure to such multinationals with substantial revenues and profits generated overseas, is the WisdomTree US Quality Dividend Growth Fund (DGRA), which has been outperforming the S&P 500 Index in 2016. A Trump win is more likely to favour US quality dividend payers for reasons described above.

Positioning strategically around a Trump win would mean considering the US small-cap equity exposure to take advantage of stronger domestic growth expectations. By contrast, if Clinton wins, a slowing economy at home would compel investors to allocate to exporter stocks or more defensively around high dividend payers. There is also more scope to underweight or allocate away from the US equities and consider exporters of Europe, who will likely benefit more from a Clinton win.

Below we summarise our key strategic views on the US elections using the UCITS ETF range.

Figure 3: Overview of how the WisdomTree UCITS ETFs may be used to position strategically around equities after the results of the US elections

Long-Term Asset Allocation with a Trump win

View on Asset class	UCITS ETF	Ticker
Bullish domestic growth biased Equities	WisdomTree US SmallCap Dividend UCITS ETF	DESE
	WisdomTree US Quality Dividend Growth UCITS ETF – USD Acc	DGRA

Long-Term Asset Allocation with a Clinton win

View on Asset class	UCITS ETF	Ticker
Bullish internation al–biased equities	WisdomTree US Equity Income UCITS ETF	DHS
	WisdomTree UK Equity Income UCITS ETF	WUKD
	WisdomTree Europe Equity Income UCITS ETF	EEI
	WisdomTree Europe Equity UCITS ETF – EUR Acc	HEDF
	WisdomTree Eurozone Quality Dividend Growth UCITS ETF – EUR Acc	EGRA

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